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FEDERAL COMMUNICATIONS COMMISSION
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October 27, 1995

William F. Caton
Acting Secretary
Federal Communications Commission
Mail Stop 1170
1919 M Street, N.W., Room 222
Washington, D.C. 20554

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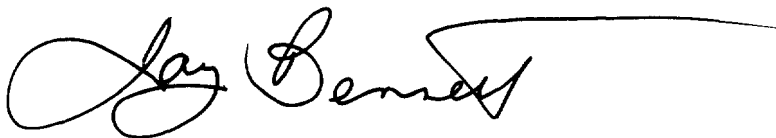
Dear Mr. Caton:

Re: *CC Docket No. 94-1, Price Cap Performance Review for Local Exchange Carriers; Treatment of Video Dialtone Services Under Price Cap Regulation*

On behalf of Pacific Bell, please find enclosed an original and six copies of its "*Comments in Response to Third Further Notice of Proposed Rulemaking*" in the above proceeding.

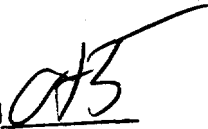
Please stamp and return the provided copy to confirm your receipt. Please contact me should you have any questions or require additional information concerning this matter.

Sincerely,



Enclosure

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Before the
FEDERAL COMMUNICATIONS COMMISSION
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OFFICE OF SECRETARY

In the Matter of

Price Cap Performance Review for Local Exchange
Carriers; Treatment of Video Dialtone Services
Under Price Cap Regulation

CC Docket No. 94-1

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**COMMENTS OF PACIFIC BELL IN RESPONSE TO
THIRD FURTHER NOTICE OF PROPOSED RULEMAKING**

I. INTRODUCTION

Pacific Bell hereby responds to the Commission's Third Further Notice of Proposed Rulemaking,¹ which seeks comment regarding the procedures for allocating costs to the video dialtone ("VDT") basket established in the Second Report and Order. We propose a *de minimis* threshold different from the one the Commission suggests, and a Part 69 allocation process based on a LEC's own VDT cost studies, rather than an arbitrary fixed allocator.

¹ In the Matter of Price Cap Performance Review for Local Exchange Carriers; Treatment of Video Dialtone Services Under Price Cap Regulation, CC Docket No. 94-1, Second Report and Order and Third Further Notice of Proposed Rulemaking, FCC 95-394 (Rel. September 21, 1995) ("Third FNPRM").

II. DISCUSSION

A. THE *DE MINIMIS* THRESHOLD SHOULD BE SET AT A DIFFERENT POINT THAN THE COMMISSION PROPOSES

The Commission proposes to set a *de minimis* threshold that determines whether a LEC must include VDT costs and revenues in its calculation of sharing or low-end adjustments. Once a LEC exceeds the *de minimis* threshold, the VDT services shall be excluded from the calculation of sharing obligations or the low-end adjustment. The Commission suggests that “the threshold . . . be set at the amount of dedicated video dialtone investment that would reduce the LEC overall rate of return by a specified amount, such as 10 or 25 basis points”² We believe the method of calculating the *de minimis* threshold should not be based on rate of return methodology.

We suggest the Commission modify its suggested threshold to provide that if a LEC’s interstate dedicated VDT plant in service investment is less than 1% of the LEC’s total interstate investment, the LEC’s VDT investment should be considered *de minimis*. There are two reasons for adopting the threshold we propose.

First, any calculation tied to the LEC’s “overall rate of return” is an anachronism from the days of rate of return regulation. To revive rate of return regulation -- even only a vestige of it -- with a product as new and competitive as VDT is inappropriate.

Second, as the Commission recognizes, the *de minimis* threshold should not be set so low that LECs making insignificant VDT investment must bear the “unnecessary administrative burden” of excluding VDT costs and revenues from its sharing and low-end

² Third FNPRM, ¶ 40.

adjustment calculations.³ The Commission acknowledges that many LECs' VDT deployment is too limited to justify this burden:

[M]any of the LECs intending to provide video dialtone will begin with small systems capable of serving a limited number of households. Thus, in the early years, video dialtone investment for at least certain LECs may well be too small to have a significant effect on the LEC's overall interstate earnings as computed for sharing and the low-end adjustment.⁴

The 1% threshold we propose will allow LECs with the small VDT investment the Commission describes to avoid the administrative burden of removing VDT costs and revenues from sharing calculations, while ensuring that LECs deploying more significant systems do not offset low initial VDT earnings against their sharing obligations. We urge the Commission to set the *de minimis* threshold at a level that does not require LECs to engage in unnecessary make-work which produces no economic benefit for ratepayers.

B. WE PROPOSE A THREE-STEP PROCESS FOR ALLOCATING VDT COSTS TO THE VDT BASKET

The Commission asks for comments on a method or factor to be used in allocating VDT costs to the VDT basket.⁵ We suggest the following three-step process:

1. Calculation Of Total VDT Amount

First, we will identify the direct and shared VDT investments, expenses and revenues following the RAO 25 subsidiary record requirements.⁶ Then we will allocate all

³ *Id.*, ¶ 35.

⁴ *Id.* (emphasis added).

⁵ *Id.*, ¶ 41.

⁶ Responsible Accounting Officer Letter 25, 10 FCC Rcd 6008 (1995) ("RAO 25"). RAO 25 sets forth specific guidance for LECs providing VDT on the requirements for accounting classifications, subsidiary records and required amendments to cost allocation manuals.

shared costs, including common company overheads, to VDT activities. The result of these cost allocations and assignments will be the total VDT amount.

2. Calculation of Interstate Portion of Total VDT Costs

Once we have determined the total amount of VDT costs, we propose to calculate the interstate portion of those costs using a process consistent with the Commission's suggestion that LECs "allocate costs to the video dialtone basket using the approach in the new services test applied in the tariff review process for setting video dialtone rates. . . ."⁷

The Commission's suggestion and our proposal for allocating state and interstate investment based on our tariff cost study are also consistent with the Commission's rulings on the appropriate separation between state and interstate services in the Telco-Cable Cross-Ownership docket. The Commission stated in its VDT Reconsideration Order that it has jurisdiction over "services involving delivery of video communications that are part of a continuous stream of communication provided at least partially by means of radio waves."⁸ The Commission further clarified that "broadcast or other radio-based video signals delivered by a LEC over a video dialtone system constitute an integral part of an interstate radio transmission service."⁹ The Commission also stated that state commissions will have jurisdiction over

⁷ Id. See also In the Matter of Telephone Company-Cable Television Cross-Ownership Rules, Sections 63.54-63.58, CC Docket No. 87-266, Memorandum Opinion and Order on Reconsideration and Third Further Notice of Proposed Rulemaking, 10 FCC Rcd 244 (1994), ¶¶ 214 et seq. ("VDT Reconsideration Order") (allowing LECs to rely on the cost support they develop for their VDT tariffs for price caps calculations).

⁸ Id., ¶ 121.

⁹ Id., ¶ 123 (emphasis added).

services which involve transmission of information services and content from video libraries or file servers located in the state to end users located in the same state.¹⁰

Using the Commission's framework, we can characterize our VDT offerings as state services or interstate services. We plan to issue tariffs for three VDT offerings -- Analog Broadcast Service, Digital Broadcast Service, and Digital Interactive Service. We currently plan to tariff two of the services -- Analog Broadcast Service and Digital Broadcast Service -- in the federal jurisdiction because both services involve the use of broadcast video signals. We plan to tariff our third VDT service -- Digital Interactive Service -- at the state level because the service involves only in-state transmission of video content from libraries or file servers to end users.

Therefore, we propose to perform a special study, based on the cost study we have conducted in support of our VDT tariffs, to determine the amount of VDT investment appropriately assigned to the interstate jurisdiction. Allocations of all other shared investments and expenses will follow the allocation of the VDT investment. If, hypothetically, our cost study demonstrates that interstate services represent two-thirds of our VDT network investment, then we will allocate two-thirds of our VDT costs to the interstate jurisdiction.

We suggest that the Commission not adopt "a fixed cost allocation factor, such as a specified percentage" for allocation of state and interstate investment.¹¹ While such an approach might be easy to administer, the differences among the LECs' VDT offerings make a cookie-cutter approach inappropriate. A fixed allocator would be arbitrary and bear no relationship to the costs underlying interstate or intrastate VDT services. Such an allocation

¹⁰ Id.

¹¹ Third FNPRM, ¶ 41.

would produce an inappropriate mismatch between revenues and costs. We believe it is most appropriate to use the costs a LEC relies upon to set its VDT rates as a basis for calculating amount it assigns to the VDT basket.

3. Direct Assignment of VDT Interstate Investment to VDT Basket

As the final step, we propose to assign the amounts derived from the foregoing process directly to the VDT price cap basket. We will not combine the VDT investment with telephony investment prior to the Part 69 allocation. Rather, we will distinguish between the VDT investment and our telephony investment at the first step of the process, and directly assign the VDT interstate investment to its own VDT basket. We believe ours is a simple and accurate means of conducting the Part 69 allocation process for VDT, and helps promote the Commission's goal of avoiding cross-subsidies between VDT and telephony.

III. CONCLUSION

We urge the Commission to set the *de minimis* threshold for VDT sharing and low-end adjustments at a reasonable level, and to allow LECs to base the Part 69 VDT allocation on their own cost studies costs rather than on an arbitrary fixed allocator.

Respectfully submitted,

PACIFIC BELL

A handwritten signature in black ink, appearing to read "Sarah Rubenstein", written over a horizontal line.

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Date: October 27, 1995